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Industrial policy in Southern African regional integration and development

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SWEDEN

1. Introduction

This paper builds on the theme of regional industrial policy addressed in a number of recent tralac Working Papers and Trade Briefs (McCarthy 2013; Sandrey 2012 and 2013; Woolfrey 2013; and Zarenda, 2012, 2013a and 2013b), and a paper in the Yearbook 2012 (Zarenda, 2013b). The intention is not to repeat what had been written in this spate of tralac documents or to present a summary review but to ask critical questions about what can realistically be expected of industrial policy in southern African integration and development. The paper is largely speculative, and to make it clear at the outset, it represents the views of a sceptic, someone who would like to be convinced that conventional industrial policy can work in the region's integration arrangements.

The interest revealed in industrial policy reflects the priority attached in the region to microeconomic intervention to allocate resources in support of the faster growth of manufacturing as a driver of economic development. In South Africa, the dominant economy in the region, there is concern about the relative decline in the contribution of manufacturing to the Gross Domestic Product (GDP), seen as a problem of the deindustrialisation of a developing economy. This concern underlies a number of policy interventions and government initiatives, and, recently, an observable move towards a more protectionist stance in national policy.

South Africa's policy positions have important implications for the smaller member states of the Southern African Customs Union (SACU) and the commitment of member states to adopt policies that will address regional inequalities and the need for the faster development of Botswana, Lesotho, Namibia and Swaziland. The 2002 SACU Agreement (2002 SACUA) is explicit about the role of industrial policy in addressing inequality among member states, to the extent of having an article (Article 38) that commits member states to develop common industrial policies and strategies in pursuance of the balanced industrial development of the Common Customs Area. SACU member states are also members of the Southern African Development Community (SADC), which means free trade within SADC but with SACU as a subgroup having a common external tariff vis-à-vis third countries.

In the larger region the member states of SADC have placed industrial development at the core of the region's development integration approach. This is embodied in both the SADC Treaty and the Regional Indicative Strategic Development Plan (RISDP). The latter can be described as a blueprint for regional integration in SADC. To give content to the important role envisaged for industrialisation in the region, SADC has adopted an Industrial Development Policy Framework (IDPF).

A discussion of industrial policy in SACU and SADC is preceded by a brief review of contextual issues covering the definition of industrial policy, in order to explain the broad nature of this microeconomic policy, and the challenges that arise if it is to be implemented by a regional integration arrangement as a regional policy. More attention is given to the SACU case than to that of SADC because of the special role assigned to industrial policy in the 2002 SACUA.

2. Defining industrial policy and its measures

Consideration of industrial policy in a regional context requires an understanding of the meaning of this ubiquitous term. The interpretation that applies in this paper has already been alluded to above: microeconomic government intervention to allocate resources to more productive use, in general in support of more rapid industrialisation, that is, a focus on manufacturing growth.[1] These efforts aimed at achieving long-run productivity improvements are argued to be justified by the existence of market failures.

Rapid industrialisation, it is generally agreed, is essential for the economic transformation of developing countries to higher levels of development. More than 40 years ago Mytelka (1973: 240) expressed a view which remains true to this day: 'Integration in many developing areas of the world is....a paradigm for industrialization'. More recently, the United Nations Industrial Development Organisation (UNIDO) (2009: 4) observed that 'industrialization is integral to economic development', further noting that '[s]carcely any countries have developed without industrializing, and rapidly growing economies tend to have rapidly growing manufacturing sectors'. It is therefore not surprising that industrialisation is seen as a principal objective of the regional integration arrangements concluded by developing countries, of which SACU and SADC are examples, and is seen to be the rationale of what has become known as developmental integration.

In Africa, structural change through industrialisation is imperative. The improvement in the growth record of African economies since the mid-1990s has been widely reported and commented on, growth that to a large extent has been the outcome of growth in mineral exports and increasing

[1] A clinical interpretation of industrial policy covers intervention across all sectors and it is not impossible to envisage an industrial policy that favours agricultural development, all depending on resources and comparative advantage. New Zealand would be an example of having an industrial policy that favours the agricultural value chain.

commodity prices, and consequently rising incomes and domestic demand. The sustainability of this growth will depend on economic diversification through industrialisation, thus creating a broad-based economic structure to drive economic growth.[2] No doubt growth in domestic demand in the wake of primary-product export growth is bound to result in some domestic manufacturing growth without having been initiated by active government intervention, but it is difficult to deny that properly designed and implemented industrial policies have an important role to play in facilitating diversified manufacturing growth, especially if this growth, as will be argued below, is to be export oriented.

The measures that can be and have been used in industrial policy cover a wide spectrum of demand- and supply-side instruments. *Demand-side* instruments refer to the external market interventions of conventional trade policy such as import tariffs, quotas and licensing, local content requirements, export taxes and export promotion measures, which may include direct and indirect subsidies. To these may be added the manipulation of the exchange rate, specifically to create an undervalued rate which protects domestic industries against imports and subsidises exports.

The regime of international trade regulations under the auspices of the World Trade Organisation (WTO) has changed substantially since earlier years when the Asian newly industrialised countries made extensive use of demand-side intervention. Currently, the use of external market intervention is severely circumscribed. Consequently the focus has shifted to *supply-side* measures. These can be classified into two categories: product market and factor market interventions (Pangestu 2002: 150). The former include policies aimed at enhancing competition and regulations that govern domestic market entry. Factor market interventions can use a variety of measures. For the labour market there are, for example, training and skill development tax incentives and subsidies, employment subsidies, labour market regulations, and wage policies. As far as the capital market is concerned there are fiscal incentives to encourage investment, both investment by domestic firms and foreign direct investment; deregulation to enhance the ease of doing business and investing; increasing the flow finance for investment through the establishment of specialised financial institutions; and targeted investment in infrastructure.

A popular development in developing countries, also in Africa, has been the tendency to offer a package of demand- and supply-side measures to industries located in designated special economic

[2] In a review of African economies' recent growth performance Kappel (2014: 7) concluded the following: 'Africa is tasked with industrialization. Direct investments need to flow with increasing intensity into industry. Only in this way can sustainable growth occur, one that is characterized by the parallel and combined development of agriculture, agro-industry, light industry, industrial zones and small and medium-sized businesses'.

zones (see Woolfrey 2013). Often these zones form part of programmes to seek a more even spatial distribution of economic activity within a country. National regional development policies are likely to depend on the encouragement of manufacturing, the most footloose economic activity, by incentivising industrial investment in lesser developed regions with relatively large populations. As will be discussed below such policies could potentially clash with efforts to promote more equal development in a regional integration arrangement that binds together a number of economically unequal member states. Earlier, the commitment in the 2002 SACU Agreement to develop common industrial policies for the sake of encouraging faster growth in the BLNS (Botswana, Lesotho, Namibia and Swaziland) economies vis-à-vis that of South Africa was noted. Such a commitment would surely call for a coordinated approach in the establishment of special economic zones within the common customs area, or for SADC within the free trade area.

Implicit to the narrative of this paper is the contention that industrial policy, to be truly effective, must be coherent in combining microeconomic intervention measures in an integrated way. When considering the range of available policy measures industrial policy is not like the pick-and -choose counter in the sweet shop where personal preferences determine the selection of sweets to suit the particular bias of a shopper. For example, if the objective is diversified, export-oriented manufacturing growth, little will be gained if manufacturers are allowed duty-free access to intermediate goods imports but have to cope with poor transport and communications infrastructure, labour market regulations that have a negative impact on competitiveness, and the absence of developed financial services and access to finance.

3. Industrial policy in regional context

What is the relevance of this view of the nature of industrial policy (as a broad range of policy measures) to integrated regional development? How can these policy measures be applied collectively to countries that participate in a regional integration arrangement (RIA)? Although member states may share the goal of diversified manufacturing growth, a moment's consideration should make it clear that developing a regional industrial policy will be a complex matter, touching on issues such as the economic diversity of the member states, national sovereignty, the degree of regional integration and the scope of the planned intervention. Below, industrial policy for SACU and SADC will be reviewed briefly to illustrate different approaches to regional policy. In this section the intention is to flag *a priori* a selection of general problems that have a cross-cutting impact on the potency of nearly all measures when applied in a regional context. The selection is based on the prominence of issues in the appraisal of industrial policy.

3.1 Policy coordination and economic polarization

With the exception of South Africa, the domestic markets of the region's economies are very small. Even the South African market cannot in terms of size be regarded as large, and, when the market of SADC is viewed in aggregate terms, its economy which in market size measured by GDP (US$575.5 billion in 2010) is significantly smaller than the GDP of the Netherlands (US$796.3 billion in 2010),[3] which in global terms is not large.

Sustainable long-term growth will therefore depend on the ability to follow an export-oriented route to higher levels of development, thus emulating the historical growth path of the fast-growing emerging economies as well as that of developed economies like the Netherlands and Germany. To establish an export base in economies that lack a diversified manufacturing sector and a vibrant business sector noted for their entrepreneurial and managerial capabilities will furthermore require foreign direct investment and in the new global economy the ability to link into global supply chains.

This brings to the fore a problem that affects all measures. The challenge is to devise policy interventions in the region in a coordinated and synchronised way and, more pertinently, to avoid an excessive competitive spirit in incentivising direct investment. Competition can be beneficial but uncoordinated investment promotion incentives to develop a manufacturing export capacity can easily lead to a race to the bottom if ineffective use is made of scarce resources (for example, depletion of the tax base) in developing countries that can ill afford such wastage.

The need for policy coordination is of particular importance in agreeing on and implementing policy measures for disparate economies. The SADC member states, and within this region the members of SACU, have economies that vary substantially in size, availability and quality of primary-sector resources, and the level of infrastructural and industrial development. In this regard South Africa stands out as a larger more diversified economy that contributes about 63% of the aggregate GDP of SADC. Nevertheless, South Africa shares with the other member states in the region a burden of large numbers of citizens that live in absolute poverty. The need for job-creating and thus poverty-reducing growth exists in all the countries but economic diversity may require different growth paths. Added to

[3] Sources respectively: http://www.sadc.int./about-sadc/overview/sadc-facts-figures/#GDP and http://www.tradingeconomics.com/netherlands/gdp [31 January 2014].

this is the challenge of harnessing the benefits of agglomeration for economic growth while coping with the impact of polarised growth in the region.

On the need for different growth paths it should be noted that South Africa forms part of the group of upper middle-income economies that falls in the category of slow-growing middle-income countries identified by UNIDO (2009: 5). In this respect and considering that many other economies in the region are low-income, an observation by Rodrik (2003: 17) becomes relevant and worth quoting: ‘The policies required to initiate a transition from a low-income equilibrium to a state of rapid growth may be qualitatively different from those required to reignite growth for a middle-income country’.

A factor that further illustrates the complexity of and need for policy coordination is the use of special economic zones, discussed earlier, as a means of encouraging industrialisation. An industrial policy for the region will require a regional perspective on the location of these zones, which would include the development of infrastructure across borders. Seen from a national perspective the growth opportunities that special economic zones could potentially provide would prove to be very attractive for South Africa in its efforts to revive industrial growth and turn around the declining contribution of manufacturing to GDP (from 22.9% in 1991 to 13.4% in 2011)[4]. But the overriding question remains: what will the impact of incentivised decentralised growth in the somewhat lame but still dominating industrial powerhouse of a polarised region be on the nascent industries of the smaller and less industrialised neighbouring countries? An industrial policy for the region will have to deal with an issue such as this.

3.2 Global value chains

The importance of dissecting and incorporating the global value chain (GVC) has become a significant feature of industrial policy analysis. For developing countries the sole requirement for industrial growth is no longer to be competitive as a low-cost producer; linking into a GVC or trade network has become a condition for rapid industrial growth. Although an imperative, being part of a global value chain is not without its problems.[5] Nevertheless, ‘the introduction of Global Value Chains into the world trading environment has forced a change in thinking regarding these operations – these now focus on activities that are integrated in a much more complex manner’ than the operations of many international firms abroad during much of the 20th century (Zarenda, 2013: 6-7). The GVC now adds a range of activities to the subcontracting of production and the fast growth

[4] Source: http://devdata.worldbank.org/AAG/zaf_aag.pdf [4 February 2014].
[5] For a short discussion of the problems associated with value chains or supply networks, see Ul Haque (2007: 5-6).

globally in what UNIDO (2009: 49) calls 'trading in tasks' as a special form of intra-industry trade. Design, production, marketing, distribution and servicing for producers and consumers are divided into elements that are spread across the globe.

The objective in this paper is to consider the inclusion of the GVC in regional industrial policy, which brings into play the two dimensions of value-chain analysis when considered in a regional context. It is important to clearly distinguish, on the one hand, the development of a value chain within a region that is managed through a regional integration arrangement (such as SACU and SADC) and, on the other hand, a value chain that operates globally.

This distinction is crucial for the incorporation of value-chain links in regional industrial policy. It is difficult to conceptualise how a regional economy governed by regional integration institutions can link into a GVC through a regional industrial policy. Becoming part of a global trade and production network is primarily a national policy issue. In a *producer-driven* value chain such as motor vehicle manufacturing, assembly and component manufacturing in South Africa for export to foreign markets, for example, is the outcome of a decision by an overseas-based multinational corporation that is likely to have been influenced by the attraction South Africa offers as location and has little to do with the fact that South Africa is a member of SACU or SADC. Also, if the marketing decision is taken to film an advertisement of a particular vehicle model in South Africa, the national availability of the required film services and the natural environment with the required scenic setting will be the determining factors that influence such a decision. This has little relevance for a policy decision that 'South African companies will be encouraged to participate ... in integrating *regional* supply chains to promote industrialisation' (RSA 2012: 120, own italics).

The crucial question for the SACU commitment to the development of common industrial policies and for the SADC IDPF is the following: how is participation in a GVC encouraged at a regional level? In questioning a place for GVC participation in regional industrial policy the intention is not to raise doubts about the contribution that appropriate regional integration and development efforts can make to a country in the region's becoming more attractive for GVC-based investment; it is merely contended that it is unlikely that the a regional industrial policy as such can make a direct contribution to GVC investment.

In contrast to producer-driven value chains and their commensurate impact on investment in southern Africa there are strong indications of the expansion of regional *buyer-driven* value chains, with the lead firms being South African manufacturers investing in the smaller neighbouring economies. In a study of Lesotho's apparel industry Staritz and Morris (2012) found that South African apparel manufacturers have since 2005/06 relocated to Lesotho in significant numbers, bringing the current number of South African-owned plants to 15, and increasing Lesotho's apparel exports (HS61-62) to South Africa from R6.25 million in 2005 to R445.24 million in 2011. From the perspective of a regional industrial policy, the primary drivers for South African investment in Lesotho, tightly linked to South African retailers, have been found to be the lower cost of labour, a comparatively flexible labour market, a more compliant union environment relative to South Africa, and proximity to the South African market which as part of a customs union can be accessed free of duty (Staritz and Morris 2012). It can also be surmised that South African manufacturers in Lesotho benefited from Lesotho's being part of the Common Monetary Agreement (CMA) which through its exchange rate regime of parity between the rand and the maloti removed the element of risk associated with exchange rate volatility.

It is questionable whether cost-driven value-chain investment can be sustainable should common industrial policies in SACU actually materialise. Labour-market policies are an inherent element of industrial policy and it is difficult to envisage that South African trade unions will accept common SACU industrial policies that will facilitate a substantial relocation of production and jobs to BLNS. This focuses attention on the likelihood of developing common industrial policies in SACU, a question addressed in Section 4.

Apart from cost-driven cross-border investment by South African firms it is also possible to envisage regional value chains that add value to primary commodities within the region. An example that illustrates this possibility is Botswana Ash (Pty) Ltd, a joint venture of the Botswana Government and a private South African firm that produces soda ash, which is used as an input by South African glass (float and container glass) manufacturers.

3.3 Trade in services

A pervasive tendency exists to underestimate the role of services in regional integration. This has an impact on the ability to design and implement a regional industrial policy.

The rigid adoption of the linear approach[6] to regional integration implies that services are only adequately addressed when a common market is formed, hence the tendency to focus on trade in goods before this advanced level of integration can be contemplated. Such an approach disregards the importance of services in their own right as income-creating activities (consider, for example, a regional approach in developing the tourism industry) and in supporting growth in the commodity-producing sectors of the economy by services such as banking, financial, logistical and communication services. The development of regional value chains will depend on the existence of an efficient service sector. Regionally integrated retail service providers can also provide a valuable conduit for the growth in the intraregional trade of goods.

Services, in contrast to goods, cross regulatory barriers and are not subject to customs duties. This implies that regulations that govern and constrain the flow of services across regional borders can restrict intraregional trade in goods in a free trade area and in this sense can be regarded as an important non-tariff barrier to trade. Adherence to the linear model in a way that does not adequately recognise trade in services ignores the variable mix of possible constituent elements of regional integration. For developing countries, the implementation of a common external tariff in moving from a free trade area to a customs union has proven to be a difficult bridge to cross. However, there is no logical reason why this should be an obstruction to investing in transport and communication infrastructure while also easing the burden of national regulations on financial services as means of facilitating intraregional trade in goods and cross-border investment.

But what is the relevance for a regional industrial policy of taking services into account? It increases the complexity of policy design in having to incorporate a mix of border-based instruments that affect the flow of goods and regulations governing the services that impact on intraregional trade and cross-border investment. The design, implementation and monitoring of this policy mix require an institutional capacity that exists in few developing countries, let alone at the level of regional organisations. This factor is discussed in the following section.

[6] The linear model portrays regional integration in sequential steps of deeper integration. It starts with a *free trade area*, covering trade in goods, followed by a *customs union* that adds a common external tariff to free trade, followed by a *common market* that provides for a free flow of labour and capital in a customs union. The final step is monetary and fiscal integration in bringing about an *economic union*.

3.4 Institutional development at the regional level

In institutional economics 'institutions' do not refer to organisations but to formal and informal sociopolitical arrangements that include elements such as property rights, regulatory structures, the judiciary, and bureaucratic capacity. There is growing consensus among students of economic growth and development that the quality of institutions is crucial and that a close association exists between institutional development and economic growth.[7]

To design and implement policy, especially a wide-ranging and coherent industrial policy, demands an understanding and commitment to legal rights and commitments as well as depth and quality in commensurate institutions such as an independent judiciary system and legal framework that can ensure contractual commitments, agreements and the security of property rights; the required regulatory structures; and quality (skilled) governance. Once an appropriate policy has been developed and implemented it needs to be continuously monitored and adaptations made where these are required. These are all challenges that can prove difficult in regional integration arrangements where the institutions of regional governance are weak and poorly supported by member states, each pursuing its own development agenda.

The real outcome of integration arrangements does not match the ambitions conveyed in the agreements, protocols, road maps and institutional arrangements of SACU and SADC. Much has been written on the relatively weak outcome of ambitious regional integration arrangements in Africa and the reasons for this[8] can primarily be traced to the complexity of using regional integration as an instrument of the diversified development of primary-producing economies and a lack of commitment by member states that do not wish to sacrifice their policy sovereignty. It can also be argued that African regional integration arrangements tend to be too ambitious, which after the conclusion of agreements tend to undermine confidence in achieving the goals adopted within the stated time frames and hence a lack of commitment. In such an environment of weak commitment the development in time of quality institutions becomes impossible.

[7] The word 'association' is used intentionally since causality cannot always be unambiguously determined. Institutions may develop endogenously as a by-product of economic growth but the view that good institutions are 'essential preconditions and determinants of growth' (Rodrik 2003: 8) has gained ground.
[8] For a succinct discussion of relevant issues see Economic Commission of Africa (2004: 32-33, 57-72).

4. SACU and SADC industrial policy

In Section 3 a broad outline of selected reasons was given why it is unrealistic to expect that a regional industrial policy will be viable and appropriate in southern Africa. The focus now shifts to SACU and SADC and the positions on industrial policy adopted for these two arrangements. The conclusion will be that that the ideas on industrial policy that are being considered by SADC are more realistic than those contained in the 2002 SACUA.

4.1 The Southern African Customs Union[9]

Common industrial policies

The 2002 SACUA is a framework agreement. It defines parameters for the operation of the customs union and a number of agreements on intentions or objectives regarding operational issues that are in time to be annexed to the Agreement. One of the objectives is found in Part Eight of the Agreement that deals with Common Policies. Article 38 on Industrial Development Policy stipulates that

- member states recognise the importance of balanced industrial development of the Common Customs Area as an important objective for economic development;
- pursuant to this recognition, member states agree to develop common policies and strategies with respect to industrial development.

It is reasonable to argue that BLNS industrialisation will in the long run depend on regional integration. Preferential market access to developed market economies such as that provided by the United States African Growth and Opportunity Act (AGOA) is important, but it is not a basis for sustainable industrial growth. For BLNS, an important benefit of SACU membership remains the potential gains to be derived from integration with the much larger South African economy. But does it necessarily follow that a commitment to develop common industrial policies is the logical requirement of being in a customs union with South Africa and that common policies are feasible and appropriate to create regionally balanced growth, or is this commitment the outcome of the confused thinking on the part of the architects of the 2002 SACUA?

SACU was established in 1910 to deal with the *de facto* economic integration of separate political entities with the dominating South African economy, enabling intraregional free trade and providing a

[9] Section 4.1 largely summarises arguments presented in McCarthy (2013).

mechanism for the distribution of the customs and excise revenue raised in the common customs area. Duty levels were decided and managed by South Africa. The customs union has since been transformed into a development integration arrangement with the adoption of the 2002 SACUA as a definitive step in transferring the management of the customs union from South Africa to supranational institutions.

What role can common industrial policies play in achieving the aims of SACU as development arrangement? Much will depend on what is meant by 'common industrial policies'. Semantically, the term would seem to mean the adoption of similar policies, which from a practical policy perspective is a nonstarter. The design of a coherent industrial policy, as argued earlier, requires a holistic approach, starting with the identification of goals and intermediate policy targets, as well as viable policy instruments, all of which depend on the nature of the economy, including elements like

- the labour market organisation in conjunction with work force characteristics (literacy levels, available skills and wage levels);
- the nature (sophistication and diversification) and size of the business sector, the manufacturing sector in particular, and the availability of a cadre of potential and existing entrepreneurs;
- the availability of natural resources such as water, fertile land and minerals;
- the existence of required service industries (finance, transport, communications, commercial, industrial and legal services);
- infrastructure;
- the institutional factors discussed earlier.

Given these factors it is difficult to imagine that the member states of SACU can have common industrial policies. Of course one can think in extreme terms and postulate deeper integration and an industrial policy for the region. After all, a customs union agreement only allows the use of a single policy instrument, namely the import tariff, which can be expanded to include selective tariff rebates and the use of the tariff as a trade remedy.[10] Because of WTO commitments on tariff bindings even the import tariff has lost much of its potency as an instrument of protection in encouraging manufacturing growth selectively.

[10] Trade remedies in the form of anti-dumping and countervailing duties can support industrial policy but they are instruments to ensure fair trade in line with WTO commitments and cannot be used as means to enact a particular industrial policy.

Nevertheless, the tariff remains an important instrument of industrial policy in those cases where viable domestic industries can be established in product lines where the applied tariff is lower than the bound rate.[11] It is well-known that the management of the SACU tariff has since 1925 served as a means of developing South African industry, serving the development needs of the South African economy. BLNS have been fairly complacent in this regard because the tariff generated revenue, the function which these member states have tended to regard as the primary role of the tariff. In the spirit of the 2002 SACUA the use of the tariff as policy instrument will require a consensus of views in a SACU Tariff Board, provided for in the Agreement (SACUA 2002: Article 11). With the Tariff Board in place South Africa will sacrifice its control over tariff management to a Board that represents all member states. Decisions on tariff changes are not taken in a policy vacuum and a prerequisite for the effective functioning of the Tariff Board will be consensus on a set of principles, derived from a shared view on industrial development, to serve as guidelines in deciding on tariff amendments, including tariff rebates.

The fact that the Tariff Board still has to be established 12 years after the Agreement has been concluded bears testimony to a lack of commitment and the problems that exist in designing management mechanisms for a customs union of largely disparate economies. It remains business as usual, with South Africa effectively managing the tariff while BLNS is 'compensated' through generous revenue distribution.

To expand the range of available policy instruments to include more than the import tariff will require deeper integration. The selective use of fiscal incentives – for example, accelerated depreciation for selected investments – forms part of the standard fare of industrial policy but this can only be used if a substantial degree of fiscal integration, beyond the current excise duty and Common External Tariff (CET) regime, exists. Fiscal integration is a building block of an economic union and it is difficult to envisage that the member states of SACU will agree to such a level of integration.

Commitment

Earlier the lack of progress with regional integration in Africa was ascribed to, among others, a lack of commitment on the part of participating states. The question can be asked whether the SACU member states have shown support for the development of common industrial policies, or for that matter, a

[11] For a review of product lines where bound rates exceed applied tariff rates, see Sandrey (2013). Sandrey (2013: 16) raises the valid point that significant policy space may in reality be less because the products serve as inputs into South African manufacturing and it will make little economic sense to raise input costs. In this paper the concern is not with the economic reality of using policy space but with the policy mechanism of using such space.

single industrial policy for the common customs area. South Africa will have to be an important driving force in moving towards such a policy position. Hence, a perusal of the official South African policy position, as revealed in relevant documents that are available in the public domain, should be informative. It will be argued that the lack of commitment revealed is likely to represent a more realistic take on unrealistic agreements that have been concluded.

Policy documents that are fundamental to industrial policy and development in southern Africa that appeared after 2002 reveal, with one exception, an absence of a serious consideration of and commitment to common industrial policies. The exception is the Department of Trade and Industry's South African Trade Policy and Strategy Framework in which SACU is portrayed as a building block of deeper integration, serving 'as an anchor in the SADC regional project' (Republic of South Africa 2010: 37) with the additional role of acting 'as a platform for harmonised engagement in wider global trade relations' (Ibid.). It is acknowledged that this vision will require 'that SACU member states forge common trade and industrial policies' (Ibid.), while developing 'a work programme that overcomes current policy gridlock by devising a strategy to build production value chains across all member states in agriculture and industry' (Ibid.). Without such a common policy vision, the document asserts, it will not be possible to strengthen SACU institutions such as the proposed Tariff Board and Tribunal and an effective and well-resourced Secretariat (Ibid.).

Similar far-reaching views are absent in three prominent policy documents. The National Industrial Policy Framework (NIPF) was introduced in July 2007 and with its successive Industrial Policy Actions Plans represents the architecture of the government's industrial development policy. Given their strategic importance one would expect at least some views on common industrial policies in SACU but these are absent. The NIPF includes in its list of Strategic Programmes one on Trade Policy in which the following is stated with regard to regional integration and SACU (Republic of South Africa, 2007: 24).

> Regional integration is a central thrust of our trade policy. South Africa will be required to devote greater attention to consolidating the SACU integration agenda and advance beyond issues of the Common External Tariff to the broader integration agenda to include *cooperation* on industrial, agricultural competition and services policy. Moreover, trade negotiations with third parties will, in future, require regional SACU approaches to all new generation issues.

It is conspicuous that the development of common policies in SACU is not raised. Instead the reference is to *cooperation* on policy, which we will argue is a more realistic perception but clearly far removed from the development of common industrial policies.

Where SACU received scant attention in the NIPF it is totally absent in the New Growth Path (NGP) launched in 2010 by the South African Government as an initiative of the new Ministry of Economic Development (Republic of South Africa 2010). The NGP emphasises the need for South Africa to reindustrialise but in an overview of policy initiatives on an active industrial policy, developmental trade policies and African development, the commitment to develop common industrial policies in SACU does not feature (Ibid.: 7, 17, 24-25). As often happens in South African policy positions on regional integration, the emphasis falls on SADC, with the NGP stating that 'South Africa will undertake initiatives to strengthen SADC and connect it with the East African Community and Comesa' (Ibid.: 25).

The National Development Plan 2030 (NDP) of the National Planning Commission has been accepted by Government as a blueprint to guide social and economic policy. The NDP contains a paper on 'Positioning South Africa in the world' with laudable objectives and proposed actions (Republic of South Africa, 2013: Paper 7). The paper reveals a strong commitment to effective regional integration in Africa and to the pivotal role that South Africa has in contributing to the economic development through regional integration, but, as will be pointed out in Note 9, is perhaps not consistently in touch with the real world of regional integration in Southern Africa. Existing agreements are not seen as cast in stone. According to the Report (Ibid.: 220):

> To take full advantage of the realignment of global politics and trade, South Africa may need to redefine its existing agreements, starting with the Southern African Customs Union (SACU) and SADC partners. These agreements should be tested for their validity and coherence and, for global bilateral and multilateral partners, affiliations and commitments. This may entail hard bargaining and potential trade-offs involving short-term realignments, gains and losses.

On the Customs Union specifically, the Commission notes that the SACU agreement is under review, stating that '[w]hile the weight of South Africa's economy has effectively reduced potential risks in the customs union, its current structure is not necessarily the best option for South Africa or its neighbours' (Ibid.: 226).[12] The Commission is aware of the fact that regional integration may entail a cost for the national economy but that regional growth will produce economic benefits. The distribution of costs and benefits is important when common industrial policies are contemplated. The Commission does not consider such policies but asks two questions that in context are relevant (Ibid.: 230): 'To what extent is South Africa willing to make concessions to protect the interests of its weaker neighbours? Should regional integration place South African interests first?' To this a third question may be added: To what extent is the protection of South Africa's weaker neighbours in its long-term interest? There can be no doubt that South Africa can only prosper in a prosperous and stable region.

The inevitable conclusion from a perusal of the South African policy documents is that the government of SACU's major economy is not committed to the development of common industrial policies. Whether this is by default or design is impossible to determine on the basis of information in the public domain. However, it is reasonable to conclude that Article 38 of the 2002 SACUA is not a guiding force in the design of industrial policy. It may be speculated that part of the reason for this is a post-Agreement understanding that the development of common industrial policies is neither appropriate nor viable because of the substantial differences in economic size, level of industrialisation and national goals between South Africa and BLNS. On national goals, for example, it is unlikely that BLNS will share the concern of the South African authorities not to develop the manufacturing sector to a position of international competitiveness on the basis of low-cost labour; hence the South African desire, consistently propagated by government representatives, to focus on manufacturing growth in higher value-added industries.

SACU review

The South African government is not committed to SACU in the format of the 2002 SACUA architecture, but is committed to a reconsideration of the SACU arrangements. The need for such a review can be traced to an intriguing situation of having to face up to the fact that the world's oldest operating customs union has to be redesigned *de novo*. As noted earlier, SACU did not come about as a planned integration arrangement; at the time of the Union of South Africa in 1910 it was an

[12] The Commission (RSA 2013) continues to argue that an immediate priority is the 'development of more effective financial transaction mechanisms to facilitate physical trade'. The Commission would seem to be unaware or at best not appreciative of the role that the CMA plays in effectively integrating Lesotho, Namibia and Swaziland into the South African money and capital market and of the close financial links between Botswana and South Africa. Add to this the statement in the report that a 'trade arrangement also exists between South Africa and SACU, whose members are Botswana, Lesotho, Namibia and Swaziland. (Ibid.: 224) and it is difficult to escape the conclusion that the Commission was less than well-informed on the real world of regional integration in southern Africa when it drafted Paper 7.

agreement concluded to deal with the de facto economic integration of the three high commission territories of Bechuanaland, Swaziland and Basutoland with South Africa.[13] The 2002 SACUA was designed to 'democratise' the customs union, relieving South Africa of its management role by transferring tariff decisions to SACU institutions while having a revenue-distribution formula in place that would maintain a revenue flow to BLNS that exceeds the amount that would be forthcoming in the absence of the customs union and its revenue-distribution formula.

This transformation is a formidable exercise. The easy option would be to disband the customs union and fall back on free trade within SADC. However, this will lead to major disruptions and instability in a region of neighbouring states noted for their porous borders and revenue deficits. But transformation to a democratised customs union will require South Africa to sacrifice control over an important instrument of industrial policy; and the question can be raised whether an economy that contributes more than 90% of SACU GDP and manufacturing output could be expected to do this, especially in view of the intentions to encourage industrial development through domestic policies? Add to this the growing concern over the fiscal cost for South Africa of the revenue transfer to BLNS. For the latter this is a major source of recurrent revenue but it is sourced from a budget that is coming under increasing pressure to meet demands for infrastructure spending and meeting the social needs of a population with more poor and unemployed people than the total population of BLNS.

It is impossible and at best difficult to unscramble eggs; this is the metaphor that comes to mind when the current situation in SACU is considered. What is clear is the need to revisit the 2002 SACUA. The idea of developing common industrial policies is out of touch with reality, the management of the tariff by the Tariff Board, yet to be established, will pose problems as far as decision making and the development of policy guidelines for tariff amendments are concerned. The distribution of tariff revenue is also a candidate for the agenda of change and in this regard the option of a structural development fund to support balanced industrial growth may be a viable proposition.

4.2 The Southern African Development Community

SADC regards industrial development as a priority and at the core of the developmental integration agenda of SADC; hence, the SADC Trade Protocol adopted in 2000 calls for an industrialisation strategy in support of the implementation of the SADC Free Trade Area as an integrated regional market that will allow economies of scale and so enhance the competitiveness of SADC firms (SADC

[13] The 1910 was seen as an interim arrangement pending the eventual incorporation of the three High Commission Territories into the Union of South Africa.

2012). Industrial development as a goal has also been given priority in the tripartite arrangement with the member states of SADC, the Common Market for Eastern and Southern Africa (COMESA) and the East African Economic Community (EAC) after having adopted industrial development as one of the pillars of regional cooperation (SADC 2012).

SADC developed the IDPF which served as the basis for consultations in member states to develop a coherent industrial policy framework and strategies in the region. The Committee of Ministers adopted the framework in November 2012.

The objective of the framework is to 'promote the development of an integrated industrial base within SADC through the exploitation of regional synergies in value-added production and export competitiveness' (SADC 2012: par. 3.4.1). It sets out areas of cooperation, recognising that industrial policy is essentially a national prerogative (SADC 2012). Common challenges are identified to be addressed by coordinated national development strategies. The premise is that the 'one-size-fits-all' approach to regional industrial policy is inappropriate in meeting the development needs of economies that differ in size, structure and resource allocation.

The IDPF emphasises three elements: the need to improve the competitiveness of industry, the promotion of industrial linkages, and in this regard the development of value chains. These are priority intervention areas that have been identified in the RISDP, which was adopted as a blueprint for regional integration in SADC in 2003 and for the Industrial Upgrading and Modernisation Programme adopted by the SADC Committee of Ministers of Trade in 2009 (tralac 2012 & SADC 2012). The IDPF recognises the importance of an efficient and regionally integrated infrastructure and of services in support of industrialisation, specifically in providing intermediate inputs into manufacturing and as a force that enhances the competitiveness of industry (SADC, 2012: par. 2.2.5 and par. 2.2.9).

To achieve its objectives the IDPF identifies a number of key intervention areas, such as sector specific strategies with a significant emphasis on value chains; the development of the skills required for industrialisation; improving infrastructure for industrial development; support for small and medium-sized enterprises; developing a mechanism for industrial financing; and promoting local and foreign direct investment and exports. The IDPF also recognises the importance of institutional capacity and proposes a five-level institutional structure ranging from the SADC Stakeholders' Forum on Industrialisation at the pinnacle to the SADC Secretariat that will have a coordinating function.

Compared to Article 38 of the 2002 SACUA, the SADC IDPF is not overambitious. The emphasis in the framework falls on cooperation and coordination in recognition of the fact that industrial policy is in the first place a national prerogative. The challenge for SADC is implementation, which will suffer if the commitment to develop the envisaged institutional structures is absent and the required skill capacities in the structures are not developed because of a paucity of resource allocations. The difficulties that may arise because important intervention areas identified at the regional level are issues that will in the first place have to be addressed at the national level. For example, it is difficult to understand what can be done at regional level to develop the skills required for modern industry and the development of an export base. Also, while regional stability and development contribute to a favourable investment environment, national policies will be crucial in encouraging local and foreign direct investment, including cross-border investment within SADC.

There are intervention areas where much can be achieved at regional level. Developing the region's infrastructure in a coordinated and integrated way immediately comes to mind as areas where regional structures can make an important contribution. Industrial financing can also benefit from regional cooperation. In the IDPF the creation of a financing window within the SADC Regional Development Fund to support industrial development has been noted (SADC 2012: par. 4.13). To this can be added increased integration of financial services to improve the availability of short-term finance for production and trade flows, as well as the regional development of the capital market to facilitate the raising of risk capital through the integration and cooperation of stock exchanges in the region.

5. Conclusion

Industrial policy is wide-ranging and has to be implemented in a coherent and integrated manner. An underlying theme of this paper is the contention that industrial policy, to be truly effective in advancing industrialisation, must be coherent in combining a range of microeconomic interventions in an integrated way. Designing and implementing an industrial policy for a regional integration arrangement of developing countries pose a number of challenges. Member states may share the goal of diversified manufacturing growth but developing a regional industrial policy will be a complex matter in having to deal with issues such as the economic diversity of the member states, national sovereignty, degree or depth of regional integration and the scope of the planned intervention. To these may be added the imperative of a commitment to regional policies and strategies, of institutional development and the existence of governing skills and capacity.

SACU has as objective the economic development of its member states. Consequently, collective decisions have to be taken on development policies and strategies that will make the most of the potential advantages of integration. This will specifically be relevant for the design, implementation and monitoring of industrial policies in support of the goal of developing all member states.

One of the most important changes introduced by the 2002 SACUA is policy integration, particularly the commitment of Article 38 to develop common industrial policies aimed at achieving the balanced development of the common customs area. The need for 'balanced development' is derived from the dominant position of South Africa and the agglomeration economies that benefit their industrial development vis-à-vis that of BLNS. But common industrial policies cannot be seen as a realistic and appropriate option. The economies of the member states are too diverse in market size, level of industrial development, resource endowments and in the sophistication and size of private business for the development of common industrial policies to be appropriate and viable. The fact that official development programmes in South Africa do not refer to the development of common industrial policies may indicate a realisation that such an approach is inappropriate.

It can be hypothesised that the provision for common industrial policies in the 2002 SACUA is linked to the formidable challenge of transforming the customs union from an arrangement with a unique history of management by South Africa to a democratised version which requires collective decision making on crucial issues such as the common external tariff. Tariff management remains an important instrument of industrial policy, which requires a consensus view on policy guidelines. To transform SACU as the world's oldest operating customs is proving to be as difficult, if not more so, as forming a customs union *de novo*, but to adopt a strategy aimed at the development of common industrial policies is bound to fail. The member states will have to revisit the 2002 SACU Agreement.

SADC has only recently adopted a common strategy on industrial development. Compared to what is envisaged in the 2002 SACUA, the point of departure adopted by SADC is sound. Industrial policy is the prerogative of each member state with the emphasis falling on coordination at the regional level and intervention in key areas. The challenge now is to implement the IDPF. It is still early days as far as implementation is concerned but if past experience is anything to go by, optimistic expectations are bound to be disappointed. The problem remains one of developing a potent and appropriate policy intervention at the regional level in a policy environment in which national policy remains supreme in crucial intervention areas. If it is further considered that institutional and administrative capacity may be lacking it becomes difficult to hold out high hopes for a regional industrial strategy.

Finally, an issue that SACU and SADC share, but to which the SADC IDPF seems to pay little if any attention, is industrial polarisation. South Africa also dominates the SADC economy. Cumulative causation and polarised development remain forces to reckon with and a regional industrial development strategy cannot ignore this.

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